

FINANCIAL SURVIVAL GUIDE



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Introduction

You think you know, but you have no idea! America is slowly sinking into its Second Great Depression of modern times. The place is every home, business, and community. The time is now. This is not a typical recession that happens to hit a bit harder or linger somewhat longer. Nor is it merely a fictional scenario conjured up by gloomy economists with a murky crystal ball.

It's the inevitable consequence of a great housing bust, a massive mortgage meltdown, and the biggest debt crisis in history.

It has already brought the largest financial failures and the greatest wealth destruction any citizen under 90 has ever experienced.

If you're still skeptical about the imminence of this chaos, you don't have to believe the former chairman of the Federal Reserve when he says we're already experiencing the worst financial crisis in 100 years. Nor must you heed the Secretary of the Treasury when he literally drops to his knees begging for more billions to save us from a financial meltdown. All you have to do is get up from your chair, open the door, and take a walk outside.

Nearly everything you see and hear will clue you in to the true plight of our time — 1 out of 10 households delinquent or foreclosed on their mortgage, 4 out of 10 upside down on their home equity, 8 out of 10 fearful of the future, and rightfully so.

You can face this!

Taking responsibility for your own situation is the first step towards achieving financial success. We all need to stop waiting for that man, woman, parent, pay rise or winning lottery ticket and recognize that the power to make positive changes in our own financial situation lies within ourselves alone.

Once we have established this, and begun our personal wealth creation journey, it's crucial that we maintain this sense of personal responsibility and independence.

Making it happen

By making short-term sacrifices we can usually gain substantial benefits over the longer term. Even though a year or so might feel like a long time to cut back on your spending or to work extra hours, the time will pass before you know it. In the meantime you will have been able to repay debt or build up your savings.

We believe the strength to make sacrifices is in all of us. If we want something badly enough, we can find a way to make it happen. The problem is, many of us put off taking action and instead accept mediocrity, persuading ourselves that any time we really needed to we could repay our debt and get things sorted.

But why wait? Why not just set a little aside each week starting today and begin repaying that useless debt now, so we can start building real wealth sooner.

It's important not to let your debt control you; get back in control of your finances, starting now. Write a list of all your personal debts, such as credit cards and personal loans and determine exactly how much you owe.

Next, establish a direct debit for each pay cycle and allocate an additional 10 to 20 per cent of your salary to repaying your debt. Of course, it's important to be sure you are meeting all of your minimum repayments to avoid late fees and a poor credit record, so don't make changes to your current repayment rates, other than to increase them.

From now on each month it's important that you read your credit card statements in full. This will remind you of all the reasons why you need to reduce your personal debt and will help you stay focused as you watch the balance come down over time.

But not all debt is bad. In fact, some debt can be a good thing, as it offers us greater exposure to an investment sooner than we would otherwise be able to achieve.

So it's a matter of understanding when we should borrow for something and when we shouldn't. We need to understand when debt is beneficial to us and when it is detrimental, because there isn't much middle ground. We'll discuss that in a bit.

How to reduce debts in bad times

In a depression, families overloaded with debts face the worst of all worlds: they miss out on major opportunities, get trapped making payments that are more onerous than expected, confront increasingly aggressive collection agencies and must abide by harsher bankruptcy laws. Therefore, if there ever were a time to get rid of debt, this is it. Here's how:

Step 1. Declare your own personal war on debt. If debt has the potential to disrupt your life and cause your family serious grief, we assure you it is not your friend. Focus all your energy on killing it.

Step 2. Attack the plastic first. Collect all credit cards in the entire household, including your own, your spouse's, and those of anyone else you're responsible for. Then grab a pair of scissors and cut them up. This is, of course the extreme way, which for many of us, proves to be necessary. Later on, we'll explain a smart way to use your credit card.

Step 3. Attack your credit card statements next. Gather all your recent statements and find the annual percentage rate (APR). At the top of each statement, write down the APR in large numbers. Then, sort the statements with the highest APR at the top, the lowest at the bottom.

Step 4. Add up your minimum monthly payments. Credit card companies deliberately require very small minimum payments. Their agenda is to let you pile up as much debt as possible so they can earn as much interest as possible. How long would it take to pay off a credit card with minimum monthly payments alone?

If you owe \$2,000 with 17 percent interest, it could take you 24 years. And on some credit cards, the compound interest you're paying could be over 35 percent! Do your best to pay them all off, even if that means borrowing from friends and relatives. If that's not possible, at least pay off the ones with the highest APR.

Step 5. Shun all new credit cards. Once you've kicked the credit card habit, don't go back. If you need the convenience of a card, get a debit card instead. But ask your bank to give you a true, pure debit card—not one that comes with a built-in credit card feature. If new, unsolicited credit cards show up in your mailbox, trash them immediately.

Step 6. Start paying down any other personal loans you may have. If you've been able to get along with, say, \$600 less per month in spending money until now, and if your circumstances don't change, you should be able to stick with it. Use it to pay down any other personal loans you may have.

Step 7. Pay down your mortgage. This is especially important if you're locked into a high rate or have an adjustable-rate mortgage (ARM). But in a depression, you must assume that even a lower, fixed-rate mortgage could become a bigger burden.

The reason: A depression usually comes with deflation, which means almost everything—including wages—goes down. Unfortunately, one of the few things that do not go down is fixed debt payments, and these can strangle borrowers no matter how favorable the loan may have seemed originally.

Your goal should be to send the mortgage company a larger monthly check than required. Then, that extra amount should be automatically deducted from your principal. If your regular payment is, say, \$2,400, send them \$3,100. You'll be surprised how much more quickly your mortgage will be paid off.

Step 8. Build up your cash savings! If you're afraid of losing your job, postpone paying down your fixed-rate mortgages until you have enough cash to cover six months of expenses.

How to save during a crisis

- During a crisis, the cost of nearly everything goes down. So your savings will buy a lot more.
- At the right time, you will be able to buy great investment bargains. The financial markets will feel like a major department store with storewide markdowns of 50, 75, or even 90 percent

- Right now, interest rates are low. But even low interest returns are better than high interest expenses. Moreover, if you wait for a time when yields spike higher, you could lock in a relatively high rate for as long as 30 years.
- Even if the depression ends sooner than expected, you will sleep nights in the knowledge that you have a cushion to fall back on in any crisis.

To achieve these goals, follow these steps:

Step 1. Determine how much you can comfortably save each month. Many people aim too high, fail, and then give up. Better to aim low and then stick with it religiously.

Step 2. Resolve to never spend a dime until after your monthly savings have been set aside. There is absolutely no expenditure (except emergencies and basic necessities, of course) that is more important than savings. This is true in good times; in a depression, it's even more so.

Step 3. Start immediately. If you do not have a savings plan in place, the sooner you begin one, the better. Even assuming just 2 percent interest, Saver A, who puts away \$10,000 per year beginning at age

25, will have \$604,020 at age 65. Saver B, who puts away \$10,000 per year beginning at age 35, will have \$405,680 at age 65. And, if you can lock in higher yields, the power of saving earlier will be greatly magnified.

Step 4. Don't confuse savings with investments. Be sure to maintain a clear separation between the two:

- Investments inevitably expose your capital to some risk; savings are designed to protect your capital.
- Investments can be in stocks, stock mutual funds, or real estate, which can go up or down. Savings should be limited to vehicles that rarely, if ever, go down in value. They prioritize the return of your money rather than the return on your money.
- With investments, it often makes sense to time the market. With savings, it does not, although key strategic changes may be needed to adapt to a major, cyclical, or historical change in the economy, such as a depression.

Avoiding the risks?

First and foremost, if you must do business with a bank, make sure it's solid financially.

Even in a broader banking crisis, depositors in the healthiest institutions will suffer the least disruption or losses.

Second, once you've found a strong bank, be sure to keep your deposits under the FDIC's insurance limit.

In the absence of a banking system collapse, the FDIC will continue to honor its guarantees and protect you from losses. And as mentioned earlier, even in a systemic meltdown, insured depositors are likely to get more favorable treatment than those who are uninsured.

Third, seriously consider moving a large portion of your savings out of banks entirely, switching them to the safest and most liquid place for your money in the modern world: short-term U.S. Treasury securities.

When you buy short-term Treasuries via a Treasury-only money market fund, you benefit from the following four advantages:

- Low fees. When a bank quotes you yields, it always quotes the yields before deducting all service fees. Because of these fees, it's almost impossible for most bank customers to collect anything near the advertised yield. In contrast, with a Treasury-only money fund,

when the fund quotes you its yield, it is invariably after deducting its fees and expenses.

- One account for both checking and savings. At banks, most customers divide their money between (1) checking accounts or savings accounts, where they give up interest; and (2) certificates of deposit (CDs) or time deposits, where they give up liquidity. In contrast, a Treasury-only money fund lets you keep nearly all of your cash assets in one single account.

You get maximum liquidity and yield on your entire balance, and you don't have to shuttle back and forth between checking, passbook savings, money market accounts, CDs, and other complex combinations. You can have one large account that meets nearly all your needs.

- Truly free checking. Nearly all banks charge you, one way or another, for checking privileges: a fee for each check you issue, a flat monthly service fee, or a combination of both. Banks say they're giving you "free checking," but require large minimum balances, paying little or no interest.

In contrast, most Treasury-only money funds do not charge you any extra fee for check-writing privileges. You can write as many checks as you want, as often as you want. This is not true for all money funds. Some levy certain charges for special services, but they're almost always lower than the charges at banks.

- Immediate liquidity. With bank CDs, there is invariably a penalty for early cancellation. With Treasury-only money market funds, there is no such thing. You can have your funds wired to your local bank overnight. Or you can write checks against it, much as you'd write checks against any bank checking account.

You might ask: The FDIC is also backed by the U.S. government, so if I have money in an FDIC-guaranteed account at my bank, what's the difference? Why should I accept a lower yield on a government-guaranteed three-month Treasury bill when I can get a higher yield on a government-guaranteed three-month CD?

Without realizing it, you've answered your own question. If the yield is higher on the bank CDs, that can mean only one thing: that, according to the collective wisdom of millions of investors and thousands of institutions in the market, the risk is also higher.

Otherwise, why would the bank have to pay so much more to attract your money? Likewise, why would the U.S. Treasury be able to get away with paying so much less and still have interested buyers for its securities?

It's because the risk is higher for CDs but lower for Treasury securities. It's because even within the realm of government guarantees, there is a clear pecking order of priorities.

- The government's first-priority guarantee: maturing securities that were issued by the U.S. Treasury Department itself.
- The second-priority guarantee: maturing securities that were issued by other U.S. government agencies, such as Ginnie Mae.
- A third priority: the Treasury's backing of the FDIC.

This is not to say the Treasury is not standing behind the FDIC at this time. Rather, the point is that, in the event of a serious financial strain on the U.S. government, FDIC-guaranteed bank deposits will not be the first in line. FDIC officials may seek to deny this, and Treasury officials may seek to pooh-pooh the distinction.

However, the wide differential in yields between CDs and T-bills tells the true story, accurately reflecting a very tangible, day-and-night difference.

Let's say I have a Treasury bill or a Treasury-only money fund. And let's say you have a CD in a weak bank. What do you have in terms of a guarantee?

You have coverage up to \$100,000 (temporarily raised to \$250,000), which in turn is backed indirectly by the Treasury. In contrast, I have a direct guarantee from the Treasury Department without any cap, and without any decision-making process that could hold things up.

What if the Government devalues the Dollar?

Throughout history, many governments have defaulted on their debts in a more subtle way—by devaluing their currency. Why are we recommending Treasuries, which are denominated purely in dollars, if one of the consequences of this disaster could be a sharp decline in the dollar's value?

The trend today is toward deflation, which means a stronger dollar. But even if that changes, the solution is not to abandon the safety and liquidity of Treasury bills. It's to separately set aside some money to buy hedges, such as gold and foreign currencies, against inflation and other unexpected events.

The big picture: In a depression, many other supposedly “safe” investments will be called into question—most stocks, of course, but also bank CDs, annuities, high-rated bonds in large companies and even widely traded tax-exempt bonds issued by cities and states. It could be a financial war zone.

But despite the wealth destruction everywhere, U.S. Treasury bills will stand head and shoulders above every other investment, returning 100 percent of your money plus interest, with your money available whenever you need it.

Profit from the decline

Fortunately, today, you can profit from a market decline without selling stocks short, and without risking a penny more than you invest. You can simply use the very same inverse exchange-traded funds (ETFs) we recommended for hedging purposes in the previous chapter.

You have the opportunity to earn greater fortunes in a bear market than most people made in great tech boom of the 1990s or in the housing boom of the 2000s. You can make that money before each major decline, during the decline, and after the decline. You don't

need a special brokerage account or even special expertise. In a moment, I'll show you how.

You don't have to be an expert to make money in the market. In fact, sometimes, those who are new to the world of investing can see the big picture more clearly than veterans who have been cocooned on Wall Street.

Whenever the government makes a new announcement to bail out this or that company or to prop up this or that credit market or to announce a new economic stimulus package, you can typically expect bursts of optimism on Wall Street. But that's probably the worst time to buy and the best time to sell. If you see that kind of a rally in the market, use it as your window to get out, or to buy contrarian investments like inverse ETFs.

Another excellent indicator is foreign currencies. When the Japanese yen is getting stronger (expressed as fewer yen to buy each dollar) that's a signal of more trouble in the U.S. market. The reason: Japan has financed a very big portion of the speculation in the United States and elsewhere. When that money rushes back to Japan, it signals that our biggest creditors are pulling out of our market. Time

for you to sell your U.S. stocks and bonds (or buy inverse ETFs) as well.

One last point: Do not expect profits all the time. In any kind of investing—in rising or falling markets—losses can and do happen.

Large Profit Potential with Inverse ETFs

With inverse ETFs, the potential for profit is quite extraordinary, even if the market is not moving dramatically. For example, between June 5 and July 15, 2008, as tech stocks fell, the inverse ETF that's tied to technology stocks enjoyed a gain of 30.9 percent, while the inverse ETF tied to the semiconductor index rose 37.2 percent. Those are large gains for such a short period of time.

Around the same time frame, stocks in the real estate sector fell even more sharply. Result: a gain of 46.1 percent in the corresponding inverse ETF between May 15 and July 15. And, due to the debt crisis, financial stocks took the biggest beating of all, driving up the inverse ETF in that sector by 106.7 percent in the same period.

As the markets became more volatile in September and October 2008, the potential gains in inverse ETFs were even larger. We saw a 61 percent gain in just 15 days as the technology sector fell between September 25 and October 10; an 89.1 percent gain in just 19 days as the real estate sector dropped between September 26 and October 15; an 89.6 percent gain in 19 days as the consumer services sector plunged between September 26 and October 15; and an 89.9 percent gain in 8 days as the financial sector slumped between October 1 and October 9.

Unfortunately, we can't go back in time to grab those profits. Nor is it possible to catch the tops and bottoms of each major move. But it's crucial to understand two things: First, unlike short-selling on margin, in each case we just cited, your risk in inverse ETFs is strictly limited to what you invest—not a penny more. And second, these kinds of gains can go a long way toward helping you through an economic crisis.

Just bear in mind that the market does not go down in a straight line; there are always going to be rallies, and sometimes they could be quite sudden. When that happens, the inverse ETFs fall in value. Like any other investment, the goal is to buy them low and sell them high. If you wind up doing the opposite, you will suffer losses.

How to Go for Profits in a Down Market

Step 1. Make sure you understand the ins and outs of inverse ETFs.

Step 2. Recognize that you can lose money in inverse ETFs.

So for this strategy, allocate strictly the funds you can afford to risk.

Step 3. Apply essentially the same tried-and-tested discipline for investing in a bull market, but in reverse:

- In a bull market, astute traders seek to buy on dips and sell on rallies. When using inverse ETFs in a bear market, do the opposite: Buy the inverse ETFs on a stock market bounce; sell them after major stock market declines.
- In a bull market, astute traders wait for temporary bouts of bad news to help drive prices down and give them a bargain-buying opportunity. They know that, as long as there are solid signs that the economy will continue growing, the stock market can climb a wall of worry.

When using inverse ETFs in a down market, do precisely the opposite: Wait for good news to help drive prices up. Then, buy the

inverse ETFs in anticipation of another decline. As long as it's clear that the economy will continue to contract, the stock market is likely to slide down a slippery slope of hope.

Step 4. Recognize that fundamental indicators that make sense in an up market may not be appropriate for a down market. For example:

- In normal times, the cheaper the stock in relation to its earnings, the more attractive it is. But in a depression, many companies have no earnings, rendering useless any measures of value based on earnings.
- Normally, the company's book value (assets minus liabilities) is another good measure. In a depression, however, as asset values fall and large debts are still outstanding, the book value is less than zero.

Step 5. Diversify among several stock market sectors while also using inverse ETFs that represent the most diverse basket of stocks.

Escape the stock market

Now, I want to show you how to escape the stock market entirely; shift to another investment world that's far removed from stocks;

and make money regardless of boom or bust, inflation or deflation, prosperity or depression.

One of the few places that's possible: in the vast global market for world currencies.

The stock market may be crashing, and it would not interfere with your ability to make money in the currency market. The U.S. economy may be mired in depression and it would still not interfere with your ability to make money. No matter what happens in the global economy or the world's financial markets, there are always continuing profit opportunities in currencies.

I don't recommend currencies for all of your money or to all investors. But at a time when nearly all other investments are going down or yielding very little, it's a good alternative—to get away from the disasters and find a separate world of investment opportunity.

In the past, this market was beyond the reach of average investors. To invest in currencies, you had to be rich, take huge risks, or both. You typically had to open special accounts, watch the markets 24/7, and immerse yourself entirely in international finance.

Today, that's no longer the case. Thanks to new, revolutionary investment vehicles, you can invest in foreign currencies just as easily as you can buy traditional investments.

The advantages of currencies are many:

1. You Never Touch a Single Stock or Bond

You do not invest in shares of companies. Your investment does not hinge on factors like the ups and downs of a company's earnings, or the vagaries of a particular CEO. Nor do you own bonds, mortgages, or other debts that can go sour.

So there's no issue with missed corporate earnings, company losses, bond defaults, or similar disasters that can drive most traditional investments vehicles into the gutter.

Just consider how many stocks have gotten killed because of poor earnings, and you'll understand how much of a relief this can be.

Even before the 2008 debt crisis, for example, United Healthcare Group missed earnings estimates by a meager 3.6 percent, and its stock promptly plunged by 32 percent. Washington Mutual missed its earnings estimates twice, and its stock plunged 70 percent.

Hundreds of others met a similar fate. This is true in good times; it's even more so in bad times. In contrast, when you invest in currencies, those events rarely have an impact on your investment.

2. You Benefit from Unrivaled Liquidity

In a depression, stock market turmoil is to be expected; and trading in many stocks—including some blue chips—can be subject to serious disruptions:

- The stocks may be hard to sell due to thin trading volume and few buyers.
- The exchange may stop all trading in the shares of companies in trouble or on the verge of a major announcement.
- Under extreme circumstances, the entire stock exchange can be shut down, potentially locking investors into serious losses.

Thanks to the high volume of trading with global participation by thousands of large institutions, these disruptions are far less likely currencies; the average trading volume in the global currency market is estimated at \$3 trillion dollars per day, many times more than the volume traded on all the stock exchanges in the world combined.

Moreover, in stock markets, that trading volume is divided among thousands of individual stock issues, greatly reducing the volume of trading in each issue. And for small- or mid-cap stocks, the volume can be especially thin.

In the currency market, we see precisely the opposite: approximately four-fifths of the trading volume is concentrated in just six major foreign currencies that trade against the U.S. dollar: The euro, The British pound, The Swiss franc, The Japanese yen, The Canadian dollar and The Australian dollar.

This means that there is vast liquidity in each major currency—a feature that's important to you for several reasons:

The large volume of trading makes it extremely difficult for any individual or institution to manipulate the market.

Prices are based on actual, current trading, making it very hard for a broker to give you a bad price.

Most important, you will rarely get trapped in a position due to the lack of buyers—or get left out of a major move due to the lack of sellers.

With stocks, you typically can get into the investment easily enough. You put your order in, and, as long as you're willing to pay up for it, you can buy the shares. But later, to get out of the stock could be another story entirely.

3. Currencies Are an Entirely Separate Asset Class

Currencies give you an opportunity for diversification beyond traditional asset classes like real estate, stocks and bonds. Plus, they give you the opportunity to continue making money during the most intense financial storms.

Example: Even following the 9/11 terrorist attacks, when the U.S. stock and bond markets were shut down for a full week, the currency market did not shut down, continuing to trade around the clock as usual.

4. There's Always at Least One Major Currency Going Up

Currencies always trade against each other in pairs: the dollar versus the euro, the euro versus the British pound, and so on. When one currency in the pair is going up, the other is going down, like a seesaw. Therefore, by definition, there must always be at least one currency that's rising in value.

For investors who feel more comfortable investing in something that's going up, the implication is that there's always a bull market in currencies. But you should feel equally comfortable investing in a currency that's going down, and the vehicles available make that possible.

5. Currencies Tend to Move in Long-Term, Sweeping Trends

Currencies are not normally impacted by the vagaries of individual stocks or industries and are usually driven by far broader, economic factors like interest rates or economic growth. Since these factors generally do not shift in direction often or abruptly, currencies can stay in a single, long-term trend for many years.

Naturally, as in any market, currencies don't go straight up or down; there will also be intermediate corrections or rallies. But as a rule, the trends in currencies tend to be more consistent and longer term, making it easier for investors to plan and profit.

The signs of a bottom in the U.S. economy and financial markets

First, look for the debt liquidation. The main debts to watch will be mortgages, mortgage-backed securities, and risky derivatives such

as credit default swaps. When these are mostly cleaned out or well on their way to being rehabilitated, it may be a time to start looking for a bottom.

Warning: If economic policy makers attempt to guarantee an unrealistic, no-loss environment for savers, if they continue to merge weak banks with strong ones, or if they insist upon sweeping bad debts under the rug, it can only delay the needed liquidation. True debt liquidation can rarely occur without bankruptcies and a full accounting for actual losses.

Second, look for a capitulation by the federal government.

This will be the critical juncture when Washington, in effect, gives up trying to save the world from financial collapses; the day they recognize they've been throwing good money after bad.

Be on the alert for a sweeping policy change that essentially means they are getting out of the bailout business. They will either forswear additional bailouts or they may even curtail bailouts that were already in the works.

Government officials will probably not announce the change in precisely those words, of course, and there may be an attempt to sugarcoat the change to avoid alarming already-panicked citizens. Third, look for a parallel capitulation by Wall Street stock analysts and bond rating agencies.

At the peak of the 1990s boom, Wall Street analysts often looked for excuses to ignore tried-and-tested formulas of stock valuation. To justify touting companies that were grossly overvalued, they said the old formulas were no longer valid.

In the future, as we approach the bottom of the market, they're likely to make the same mistake again, but in reverse. Many will have sold all their own stock. They will be playing the market to profit from the decline or they'll be looking to drive prices lower so they can buy at even cheaper levels.

Again, they will say that traditional valuation models are no longer valid—this time to justify panning the shares they used to tout. Stocks that seem undervalued, they'll argue, are really “worthless.”

At Wall Street's rating agencies, you may see a similar pattern. Instead of just piecemeal downgrades, watch for the day when the

rating agencies revise their rating scales or models across the board, with the net effect of downgrading, in one fell swoop, the entire universe of companies or investments they cover.

Fourth, you should see similar signs of capitulation among people you meet on a daily basis:

- Real estate agents, who forever were saying “buy, buy, buy,” will warn you to avoid the purchase of houses, condos and land like the plague.
- You will see a major change in people’s perception of prices, especially in the real estate area. At one point, they will still be saying, “Wow! Everything is so darn cheap, it couldn’t possibly get any cheaper. This is THE best time to buy.” But one morning, they will wake up and exclaim: “You know what! We got it all wrong.

Nothing is really cheap right now. It’s the damn prices they used to charge that were so ridiculously expensive. This is obviously the worst time to buy.”

- Nearly everywhere, you will note a switch from hear-no-evil optimism to apocalyptic pessimism. You’ll see respected Wall Street analysts advising investors to avoid stocks like the plague. You’ll see the establishment press ask if this is “the end of civilization.” You’ll

even hear your friends wondering out loud if the world is, indeed, coming to an end.

Don't be swayed! Yes, there are bound to be some events that appear to lend credence to the direst of prophecies. It may indeed seem like the end of the world in some ways. But that's when it will be the time for you to fulfill the promise you made me in the first pages of this book—to look beyond the darkness and recognize that you're actually near the end of the tunnel.

Fifth, be on the lookout for a watershed event.

No one can define ahead of time what the watershed event will be, but it could be:

- A change at the helm of the Federal Reserve and a radical shift in monetary policy.
- Major reforms in the structure of foreign currency markets.
- In an extreme scenario, a temporary shutdown not only of the banking system but also of nonessential production.

No matter what, to be a true watershed event, it must make no pretense of rescuing debtors or saving lenders. Any major attempt to do so would merely imply a perpetuation of the bailouts, no end

to the needed debt liquidation process, more false bottoms and more false rallies.

Don't miss this opportunity

When you reach a bottom in the markets, there will be no scarcity of bargain opportunities. The critical questions will be:

Do you have the cash to buy them? If you're counting on raising the cash then—through the sale of other assets or by borrowing the money—you could be very disappointed. There could be virtually no buyers for your assets at a price that would bring you meaningful value. Credit will be practically nonexistent. You must have the cash ahead of time.

Which investments should you buy first? Go for the highest quality across the board. In stocks, that means you won't have to hunt among the small, innovative companies selling for pennies.

The best, most established blue chips will be cheap enough. In bonds, there will be quite a few high-quality issues to choose from. And in real estate, you'll have your pick of the choice properties in the best locations.

Should you jump at the opportunity to buy everything you can lay your hands on? No. In the first phase of the recovery, you're better off starting slowly and investing prudently.

Since you're confident it's the big bottom, should you hold on no matter what? No. Although you have every reason to believe it's the bottom, suppose you're wrong. Set reasonable risk limits, such as 10 or 20 percent of your investment.

Should you stick mostly with the stock market? Not at all. It's quite possible that other asset classes will be the better place to start.

Basic principles for buying at the bottom

Principle 1. The biggest payoff from a market decline or deflation is having the cash to buy real estate, stocks, bonds, gold, and other assets when they've reached a bottom. That, in turn, requires the courage and stamina to take your money out of the market now, put it away, let it sit there, and then pull it out to deploy at the right time to buy true bargains.

Principle 2. After a historical decline, the best time to buy something is when virtually no one else wants it. Wait until people's emotions

are so powerful they forget the original reasons they started selling in the first place. Wait until people are selling just for the sake of selling. Don't trust the public mood in the worst of times any more than you would in the best of times. When everything looks the blackest, it could be the time for a real recovery.

Principle 3. It's a mistake to fly by the seat of your pants.

Use a benchmark—an indicator you can rely on.

How to Invest in Gold in a Crisis

Gold can be an excellent investment at the right time; it can also be a high-risk investment at the wrong time. I suggest you follow these basic guidelines:

1. Don't become too fixated on the glitter of gold as a monetary metal or a safety haven. Although those qualities can help support gold prices to some degree and for some period of time, history proves that they are no match for falling demand, abundant supplies, and deflation. Therefore, you should not accumulate large amounts of gold as a substitute for cash or savings.

2. Regardless of some theories to the contrary, the hard-nosed reality is that gold is generally a good investment in inflationary times but a bad investment in deflationary times. As long as deflation prevails, invest no more than 5 percent of your liquid assets in gold. Later, following government measures and watershed events to end the deflation, it may be time to expand your holdings.

3. After the deflationary forces are spent, there should be a new opportunity for gold investors. The fundamental signals should not be very different from the timing for buying other assets like stocks and bonds. As an additional signal, remain on the lookout for deliberate efforts by the authorities to cheapen the dollar and push prices higher.

Here are several alternative vehicles for investing in gold:

1. Gold-based exchange traded funds (ETFs). These are the handiest and most flexible vehicles. A gold ETF invests strictly in gold bullion. They are liquid, require no maintenance by the investor, and are traded on the major stock exchanges. Best of all, gold bullion ETFs do not require you to take delivery of physical gold and store it.

2. Physical gold. You can buy ingots, gold bars in many sizes, and gold bullion coins. We generally do not recommend rare gold coins. It's highly complex, and more like investing in art.

For physical gold, your best choice is gold ingots and bars. Gold bullion coins, like the American Eagle, are nice to look at, but dealers charge a premium of 4, 7, or even 8 percent for their purchase. The premium includes the cost of the U.S. Mint's charges to make the coin, plus the dealer's commission. As a rule, it's not worth it.

You can get more gold for your money every time you buy ingots or bars than when you buy gold bullion coins. If you were to buy, say, 10 ounces of gold at \$800 per ounce, it would run you just a tad over \$8,000. But if you were to buy 100 one-ounce gold American Eagles, you'd pay over \$8,500 for the same amount of gold. The same applies to Canadian Maple Leafs, Mexican Peso gold bullion coins, and the South African Krugerrand.

That's why, at the right time, we prefer ingots and bars, especially the 1- and 10-ounce ingots, and for larger purchases, the 32.15-ounce kilo bars. They're relatively easy to buy and easy to store. Just make sure you are buying what's called "four nines fine" gold, meaning 99.99 percent pure gold. The most common hallmarks are

Johnson Matthey, Engelhard, Credit Suisse, and Pamp. Most reputable dealers carry these ingots and bars in these hallmarks or can readily acquire them for you.

Who do you buy from? Choose a dealer based primarily on the quality of the service. Then establish a long-term relationship with one or two.

3. Gold mining shares. Favor gold mining mutual funds over picking individual gold shares. The reasons are obvious: you get diversification and a professional manager. Picking individual gold mining shares can offer greater returns, but also more risk.

Building New Fortunes

As the world economy recovers and you pursue the opportunity to build new fortunes, it's vital that you do so without missing a beat or suffering a major setback. Here are the guidelines to follow:

Keep your priorities straight

Aim first for savings and capital preservation, second for growth; and last for speculative profits.

Controlling risk is just as important as maximizing gains

Profit potential can be an important driver of your ultimate success. However, controlling your risk is actually more important.

For investments that expose you to large potential losses, use stop-loss orders. If the value of your stock or ETF falls, there is no guarantee that you will get a price that corresponds exactly to the stop-loss level you specify. But it should help protect your capital—either to prevent a larger loss or to protect an open profit.

Diversify beyond the stock market by investing in various asset classes—including a large allocation to Treasury bonds at the right time, plus, as economic prospects improve, high-grade corporate bonds, solid dividend-paying stocks, precious metals, real estate, and even commodities or foreign currencies.

If you speculate, use only money you can afford to lose. Far too many investors speculate with the keep-safe portion of their money. They fail to realize that speculation can ruin them just as easily as it can deliver big rewards.

Do not use funds that you'll need for emergencies, your children's or grandchildren's education, basic necessities, retirement living expenses, or long-term care. If you find yourself counting on the

expected gains in order to make your financial plan a success, you have probably exceeded your limits. Even if you do have enough capital, do not speculate if you find yourself losing sleep over it.

Keep your emotions in check

Treat investing as a business. It's not a game. Consider your income as revenues. Categorize and keep track of your expenses, including broker commissions and fees, as you would in any business. The more you do so, the more objective you will be about every aspect of your money.

Review your financial position monthly. This is especially important in tough times. Do it much like you would review your business's monthly financial statements.

Don't hesitate to change your strategy as needed. If the investment is not working for you, seriously consider changing your strategy.

Especially if you trade actively, reduce your commission costs to the bone

Consider this scenario: You're not a buy-and-hold investor. But you're not an active trader, either. Starting with \$100,000 in your brokerage account, you buy 20 different securities, with an average

initial value of \$5,000 each. Then, you buy and sell each one only twice a year, with an average profit of 5 percent per trade before commissions. With consistent profits like those, you'll retire rich, right? Not necessarily.

According to a survey of broker commissions we conducted, if you're paying top-dollar commissions (actually charged by 27 percent of the firms in our survey), your entire \$100,000 will be totally wiped out by commissions by the end of year nine.

You can avoid disaster simply by using a broker who charges you the average commission rate. But, assuming the same scenario above, the results are still disappointing. All you'd make is a meager \$21,675 in profits after 10 long years with no losses.

The only way to make good money trading semi-actively in the stock market is to find brokers with commissions on the low end of the scale. In the above scenario, instead of just \$21,675, you'd have \$108,374 in profits after commissions. In other words, just by switching from average commissions to low commissions, you'd multiply your profits by nearly five times. Bottom line: Either trade less actively, or shop more pro-actively for low commissions.